House Budget Committee
Democratic Caucus
U.S. Rep. John Spratt ■ Ranking Democratic Member

214 O'Neill Building • Washington, DC 20515 • 202-226-7200 • www.house.gov/budget_democrats

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President Clinton's Revised Budget for Fiscal Year 2001

On Monday President Clinton released the Mid-Session Review of his 2001 budget. The ten-year figures in his new budget reflect a substantial improvement in the budget forecast, and also include two major policy changes.

First, projected surpluses increase by more than $1.3 trillion over ten years.

Second, the President proposes to expand his Medicare package by $166 billion over ten years, partly by improving the prescription drug package, and partly by scaling back previously proposed Medicare savings and offering increased reimbursements for Medicare providers.

Third, the President proposes a $500 billion, ten-year "Reserve for America's Future." He suggested that the next president and future congresses should debate the best uses of the fund — additional debt reduction, program increases, or tax cuts.

The President makes a package offer to the Republican Leadership containing three elements:

- ***Medicare off budget*** **—** The offer includes treating the Medicare Part A trust fund (the Health Insurance or HI trust fund) as fully off budget. The stated purpose is to define the surpluses in that trust fund as being available only for debt reduction.

- ***The President's Prescription Drug plan*** **—** The President's Medicare-related policies in total cost $264 billion over ten years; in addition to regular and catastrophic prescription drug benefits, they include other Medicare proposals such as the buy-in, increased reimbursements to providers, and savings from modernization. (See Part 3 of this analysis for a more detailed description.)

- ***A Republican "Marriage Penalty" bill*** **—** If the Republican Leadership accepts the President's Medicare proposals above, the President will accept a Republican bill similar in size to the $248 billion bill reported by the Senate Finance Committee. However, the President's new budget includes $73 billion for marriage penalty relief, much like his February budget.[1] Thus, the extra $175 billion cost of the Senate Finance bill would presumably come from the Reserve for America's Future, leaving roughly $325 billion

[1] This amount includes proposals specific to the marriage penalty and also an expansion of the EITC and a general increase in the standard deduction.

Part 1: The President's New Budget

The federal budget can be divided into three pieces: the Social Security Trust Fund, treated as "off budget" since 1990[2]; the Medicare (HI) Trust Fund, which the President now treats as "off budget;" and all other federal programs, which are "on budget."[3] Consequently, there may be considerable confusion about which parts of the budget people mean. This memo will therefore show all three pieces of the budget, as well as the totals, in each of the tables.

Table 1 shows the surpluses in the new baseline — the budget without any new program increases or tax cuts. (This projection assumes appropriated programs will grow only with inflation.)

Table 1: Projected Surpluses in the President's Current Services Baseline
surpluses in billions of dollars

	Social Security	Medicare (HI)	On Budget	Total
2001	160	30	49	**239**
2001-2005	958	179	360	**1,497**
2001-2010	2,320	403	1,470	**4,193**

The President's budget proposes policies to reduce these surpluses, to some extent, by increasing some federal programs and by cutting taxes. Nevertheless, the vast bulk of the surpluses — $2.9 trillion over ten years — are saved and therefore automatically used for debt reduction. (The Treasury uses surpluses to redeem debt whether or not Congress specifically tells it to do so.) The President's programmatic and tax proposals have little costs in 2001.

Table 2 shows the cost of the major proposals over five and ten years. As Tables 2 and 3 show, the President *reduces* costs in the Medicare (HI) trust fund by $144 billion over ten years. This is accomplished mainly by transferring $115 billion of on-budget surpluses from the general fund to the HI trust fund over ten years. The first result of transferring surpluses to the HI trust fund is to extend its solvency until 2030. The second result is that the remaining on-budget surplus as newly defined is further reduced, to $49 billion. Thus, the President takes *two* actions to lock up portions of the projected surplus for debt reduction: he reclassifies Medicare (HI) as off budget, and he transfers most of the remaining on-budget surplus to Medicare, taking it off the table.

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[2] The Postal Service Fund was also defined as an off-budget federal agency in 1990. For convenience, the President's new budget and this analysis combine Social Security and the Postal Service under the heading "Social Security." OMB expects the Postal Service fund to run a $3 billion deficit over the next ten years, gradually running down its current balances.

[3] Other federal programs include those financed by the general fund, and also trust fund programs such as other parts of Medicare, Highways, Superfund, and Civilian and Military Retirement.

Table 2: Spending and Tax Proposals in the President's Budget
In billions of dollars; minus signs reflect costs, which reduce projected surpluses

		Social Security	Medicare (HI)	On Budget	Total
Medicare[4]	— 5 years	0	-9	-84	**-93**
	— 10 years	-1	-8	-255	**-264**
Transfers to HI[5]	— 5 years		45	-45	**0**
	— 10 years		115	-115	**0**
Other programs[6]	— 5 years	-1	1	-27	**-27**
	— 10 years	-3	3	-122	**-122**
Net tax cuts[7]	— 5 years			-5	**-5**
	— 10 years			-140	**-140**
Reserve	— 5 years			-123	**-123**
	— 10 years			-500	**-500**
Debt service	— 5 years		12	-48	**-36**
	— 10 years		34	-290	**-256**
Total	**— 5 years**	**-1**	**49**	**-332**	**-284**
	— 10 years	**-4**	**144**	**-1,421**	**-1,281**

[4] This line includes Medicare benefits for prescription drugs and catastrophic coverage (including its Medicaid costs), the Medicare buy-in, provider increases, and Medicare savings. It can be seen that almost all of the ten-year $264 billion in Medicare costs fall outside the HI (Medicare Part A) trust fund. Specifically, the prescription drug benefit and catastrophic benefit are proposed as a new Part D of Medicare.

[5] The proposed transfers from the general fund to the HI trust fund are *costs* of the on-budget general fund, which is why they are shown with a minus sign in the "on budget" column. At the same time, they are *receipts* of the HI trust fund, which are akin to savings in that they make the HI trust fund more solvent. That is why they are shown with a plus sign in the "Medicare (HI)" column.

[6] This line includes other entitlement costs, primarily to improve access to S-CHIP and Medicaid, discretionary costs, and the refundable portion of proposed tax credits.

[7] As noted, the new budget does not include the President's offer to increase the size of marriage penalty relief to roughly $250 billion over ten years.

Table 3 below combines Tables 1 and 2. It shows how the ten-year baseline surpluses displayed in Table 1 are reduced by the sum of the proposed policies in Table 2. The ten-year surpluses called for by the President are the result. As can be seen, the unified budget surpluses in his budget total $2.9 trillion over ten years. According to the new budget, these surpluses will be sufficient to pay off all the outstanding debt held by the public by 2012, with a few hundred billion dollars to spare.

Table 3: Summary of the Ten-Year Plan
in billions of dollars

	Social Security	**Medicare (HI)**	**On Budget**	**Total**
Baseline surpluses	2,320	403	1,470	**4,193**
Budget proposals (costs shown as minus)	-4	144	-1,421	**-1,281**
Resulting surpluses / used for debt reduction	2,317	546	49	**2,912**

Part 2: Changes Since the February Budget

The President's new budget differs from his February budget in five ways:

- Projected baseline surpluses have been reestimated upward by $1.3 trillion, largely because revenues are expected to grow even faster than previously thought.[8] Of the improvement, $148 billion is in Social Security, $180 billion is in Medicare (HI), and $948 billion is in the rest of the budget.

- The President increases the cost of his Medicare proposals by $166 billion over ten years: $40 billion is to increase reimbursements to providers, $33 billion is to scale back the savings in Medicare previously planned, $35 billion is to formally incorporate a catastrophic prescription drug benefit into his budget[9], and $58 billion is to expand the proposed prescription drug and catastrophic benefit.

- The President increases his target for discretionary programs by $19 billion over ten years, although there is no increase for 2001. His ten-year total is now virtually identical to current services.

- The President reduces the proposed transfers from the general fund to the Medicare (HI) trust fund, from $299 billion over ten years in his February budget to $115 billion over ten years in his June budget.

- As a consequence of the major changes — the increase in the Medicare proposal and the new Reserve for America — debt service costs are increased as well.

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[8] It should be noted that CBO is expected to release its new baseline shortly, and is likewise expected to project faster revenue growth and greater surpluses. Based on material distributed to its economic advisors earlier this month, CBO's upward reestimate and resulting baseline surpluses may be slightly larger than OMB's.

[9] Although the February budget mentioned $35 billion for a catastrophic prescription drug benefit, it was not incorporated into the budget figures in February.

Part 3: Medicare

The President's Revised 2001 Budget for Medicare

Over ten years (2001-2010), the President's revised 2001 budget increases net Medicare spending by $166 billion more than the February budget. Overall, net Medicare spending increases by $264 billion over ten years relative to current law under the revised 2001 budget.

Over the ten-year period, the revised budget dedicates a small portion of the additional surpluses to improving the original Medicare budget by: 1) enhancing the Medicare prescription drug benefit and the accompanying catastrophic protection ($93 billion total — the original $35 billion reserve fund plus $58 billion); 2) eliminating some of the provider payment savings required by the Balanced Budget Act of 1997 (BBA) ($40 billion); and 3) eliminating a portion of the provider savings proposed in the February budget ($33 billion).

Resources Dedicated to Medicare Benefits: Revised 2001 Budget Compared with February 2001 Budget

	Ten Years
Prescription Drugs & Catastrophic Protection	**+ $93 B**
Provider Payment Restorations	**+ $40 B**
Elimination of Some Savings Proposals	**+ $33 B**
Total Net Medicare Resources	**+ $166 B**

Enhanced Medicare Prescription Drug Benefit with Catastrophic Protection

The President's enhanced Medicare prescription drug benefit continues to provide a voluntary drug benefit through the Medicare program. All beneficiaries are guaranteed a defined, accessible, stable benefit for the same premium. Unlike private insurance plans, the Medicare prescription drug benefit remains available in all market areas and premiums do not vary geographically.

- ***Drug Benefits Begin in 2002 —*** The revised budget establishes the Medicare prescription drug benefit in 2002 instead of 2003, as specified in the February budget.

- ***Catastrophic Protection Begins in 2002 —*** The revised budget provides for catastrophic protection in 2002 instead of 2006, as specified in the February budget. In addition, the revised budget specifies an annual limit of $4,000 on a beneficiary's out-of-pocket drug costs. In subsequent years, this stop-loss protection is indexed to drug inflation.

- ***Low Monthly Premiums*** **—** Even with the improved benefits included in the revised budget, the monthly premiums are the same as those announced in the February budget: $25 monthly in 2002 rising to about $50 per month in 2009.

- ***Basic Drug Benefit*** **—** Like the February budget, the revised budget provides a voluntary outpatient prescription drug benefit available to all Medicare beneficiaries. The drug benefit provides first dollar coverage, pays half of beneficiaries' prescription drug costs up to $5,000 when fully phased in, and provides protections for low-income people.

- ***Special Payments to Managed Care Plans in 2001 for Drug Coverage*** **—** The revised budget provides direct payments to managed care plans in 2001 to help plans continue to offer prescription drug coverage. A subsidy is available if a plan offers drug benefits of at least $2,000 with a 50 percent coinsurance. These payments total $2 billion in 2001.

Provider Payment Restorations

The President's revised 2001 budget increases Medicare and Medicaid provider payments in order to eliminate some of the savings required by the Balanced Budget Act of 1997 (BBA). The provider payment restorations increase Medicare and Medicaid spending by $21 billion relative to current law over five years (2001-2005), and by $40 billion over ten years (2001-2010). Only $300 million of that $40 billion is for Medicaid restorations.

The provider payment restoration package includes immediate provider increases in 2001 and a pool of funds for unspecified restorations. The unspecified pool totals $11 billion over five years and $21 billion over ten years. These funds may be used for other revisions in BBA policies.

Highlights of Specified Provider Payment Restorations

- **Full Update Adjustments —** Prospective payment system hospitals, home health agencies, and nursing homes
- **Indirect Medical Education Payments —** Freeze at 2000 level, prevent further reduction for 2001
- **Medicare Disproportionate Share Hospital (DSH) Payments —** Repeal 2001 DSH cut
- **Medicaid DSH Allotments —** Freeze DSH allotments at the 2000 level for 2001
- **Home Health Agencies —** Delay the scheduled 15 percent cut
- **Nursing Homes —** Delay by one year the imposition of nursing home therapy caps (until January 2002)

Most of the specified provider restorations are one-year fixes restoring inflation adjustments for 2001 or delaying further payment reductions. The major restorations specified in the revised budget include: 1) providing full update adjustments for prospective payment system hospitals, home health agencies, and nursing homes; 2) freezing further reductions in indirect medical education payments for 2001; 3) repealing Medicare disproportionate share hospital (DSH) payments reduction for 2001; 4) freezing Medicaid DSH allotments for 2001; 5) delaying the 15 percent cut for 2002 for home health agencies; and 6) delaying the imposition of nursing home therapy caps until January 2002, an additional year. The revised budget does not include specific restorations for managed care organizations although some of the funds from the unspecified pool ($11 billion over five years and $21 billion over ten years) could be used for that purpose.

Elimination of Medicare Savings Proposals from the 2001 Budget

The revised 2001 budget eliminates some savings proposals included in the February budget. The elimination of these proposals reduces the net Medicare savings in the revised budget by $33 billion over ten years (2001-2010) relative to the February budget level.

The revised budget does not include the traditional provider payment reductions for 2003-2008 (the so-called BBA extenders) included in the February budget. In addition, the revised budget no longer includes the repeal of the bad debt policy, the preferred provider organization proposal, or the repeal of the Balanced Budget Refinement Act managed care risk adjustment policy. (See the web page of the House Budget Committee Democrats for a summary of the President's 2001 February budget, *http://www.house.gov/budget_democrats/pb01sum.pdf*.)

The revised budget retains other savings proposals from the February budget that are associated with the Administration's Medicare modernization proposals. These include the competitive defined benefits proposal for managed care plans and other Medicare fee-for-service proposals described by the Administration as producing long-term efficiencies. Other policies improve efforts to prevent, detect, and reduce fraud and abuse in the Medicare program. A description of these and other savings proposals is also contained in the Internet document cited above on the web page of the House Budget Committee Democrats.